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**REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN  
PARLIAMENT**

**Member States' Replies to the European Court of Auditors' 2013 Annual Report**

{SWD(2015) 18 final}

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# **REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT**

## **MEMBER STATES' REPLIES TO THE EUROPEAN COURT OF AUDITORS' 2013 ANNUAL REPORT**

### **EXECUTIVE SUMMARY**

This report is an analysis of the Member States' replies to the European Court of Auditors' (the Court) annual report for budgetary year 2013 and fulfils the obligations defined in Article 162 (5) of the Financial Regulation<sup>1</sup>.

The Court's annual report for 2013 stated that the consolidated accounts were free of material misstatements and that revenue and commitments taken as a whole were legal and regular. The Court's audit also concluded that overall, payments were materially affected by error and that the supervisory and control systems were in general, partially effective. The audit results showed that overall the estimated error rate was 4.7 %, down by 0.1 percentage points on last year's rate, but still above the materiality level. The Court also pointed out that a significant positive factor in 2013 was the increased impact of corrective measures applied by the Member States and the Commission. In addition, the Court's audit also revealed that for a large proportion of transactions affected by error in the shared management areas, authorities in Member States had sufficient information available to have detected and corrected the errors before claiming reimbursement from the Commission. Policy areas rural development, environment, fisheries and health as well as regional policy, energy and transport had the highest estimated error rate - 6.7 % and 6.9 % respectively.

During its 2013 audit the Court identified specific categories of quantifiable errors in shared management which contributed significantly to the most likely error rate for the policy areas concerned. In the policy area "Agriculture: market and direct support" (chapter 3), overstated number of eligible hectares or animals and ineligible beneficiary/ activity/expenditure together contributed 80 % to the most likely error rate.

In Regional Policy, transport and energy serious errors in public procurement accounted for 45 % of all quantifiable errors and made up approximately 39 % of the estimated error rate for the policy domain. In the policy area Employment and Social affairs errors related to public procurement breaches accounted for 7 % of all errors, which shows that the risk of non-compliance with public procurement is still relevant.

In chapter 3 of its annual report the Court reported on the systematic weaknesses in the Land Parcel Identification System (LPIS) stemming from incorrect assessment of the eligible land in LPIS databases. The Member States concerned were therefore requested to provide information on whether databases were updated and additional measures taken by them to solve recurrent problems. All Member States concerned replied that they could now guarantee that LPIS databases are updated on a regular basis and that the LPIS ensures a correct assessment of eligibility of land, and systematically detects over-declarations.

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<sup>1</sup> Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002. OJ L 298, 26.10.2012, p. 1.

Member States were asked whether they were in a position to state that their control system had addressed the recurrent deficiencies identified by the Court in relation to: agri-environmental commitments, ineligible beneficiaries, non-respect of procurement rules and ineligible support for early retirement. The Member States concerned stated that they had addressed all or nearly all the identified recurrent deficiencies.

Regarding the question on public procurement breaches, nearly half of all Member States responded that they had identified systemic issues related to public procurement and that they have taken preventive measures in this context.

The report examined replies to questions on Member State **accountability** with the focus on management and national declarations, management verifications and the role and importance of the Court's assessments.

76 % of Member States stated that mandatory management **declarations** could have a positive impact on the prevention, detection and correction of errors by Member States. A sizable proportion of Member States (86 %) regarded the results of the Court's assessments as useful and contributing to their own assurance of the legal and regular use of EU funds. On the subject of the usefulness of national declarations, just over half of all Member States responded favourably.

Finally, in its 2013 report, the Court found that for the 2007-2013 programming generally the focus was more on the need to spend EU funds in compliance with rules and that the focus on performance was limited. In this year's questionnaire Member States were asked how they ensured that **performance** was a key element in the use of EU funds and what measures had been put in place to monitor programme and project performance. A significant majority of Member States provided comprehensive replies to these two questions. The use of criteria, indicators and evaluations are the means by which many countries ensure performance is a key element. In terms of monitoring of performance, progress reports, control measures, evaluations and tracking of indicators are among some of the more common measures used by Member States.

# **REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT**

## **MEMBER STATES' REPLIES TO THE EUROPEAN COURT OF AUDITORS' 2013 ANNUAL REPORT**

### **1. Scope of the Report**

Article 162 (5) of the Financial Regulation states that as soon as the Court has transmitted its annual report, the Commission shall inform the Member States concerned immediately of the details of that report which relate to management of the funds for which they are responsible. Member States should reply within sixty days and the Commission then transmits a summary of the replies to the Court, the European Parliament and the Council before 28 February of the following year.

Following publication of the Court's annual report for the budgetary year 2013, the Commission duly informed Member States of details of the report. This information was presented in the form of a letter and three annexes to be completed by each Member State, as well as the accompanying guidelines on the preparation and presentation of replies to the questionnaires. Annex I was a questionnaire on the paragraphs referring to the individual Member States; annex II was a questionnaire on audit findings which refer to each Member State and annex III was a questionnaire on topical findings related to shared management for DAS 2013.

For this year's report, three main themes have been identified. They are as follows: 1) Main quantifiable errors in shared management, 2) Enhanced accountability of Member States – sound financial management, and 3) Enhanced accountability of Member States-towards a genuine culture of performance. The report is also accompanied by a Staff Working Document (SWD) which comprises Member States' replies to annexes I and III.

### **2 Key features of the ECA 2013 report**

The Court's annual report for 2013 stated that the consolidated accounts were free of material misstatements and that revenue and commitments taken as a whole were legal and regular. The Court's audit also concluded that overall payments were materially affected by error and that the supervisory and control systems were in general partially effective<sup>2</sup>. The audit results showed that overall the estimated error rate was 4.7 %, down by 0.1 percentage points on last year's rate, but still above the materiality level. The Court pointed out that a significant factor in 2013 was the increased impact of corrective measures applied by the Member States and the Commission. According to the Court's report if these measures had not been applied to transactions sampled, the estimated error rate would have been 1.6 percentage points higher<sup>3</sup>.

Policy areas rural development, environment, fisheries and health as well as regional policy, energy and transport had the highest estimated error rate - 6.7 % and 6.9 % respectively. In addition, the Court's audit also revealed that for a large proportion of transactions affected by error in the shared management areas, authorities in Member

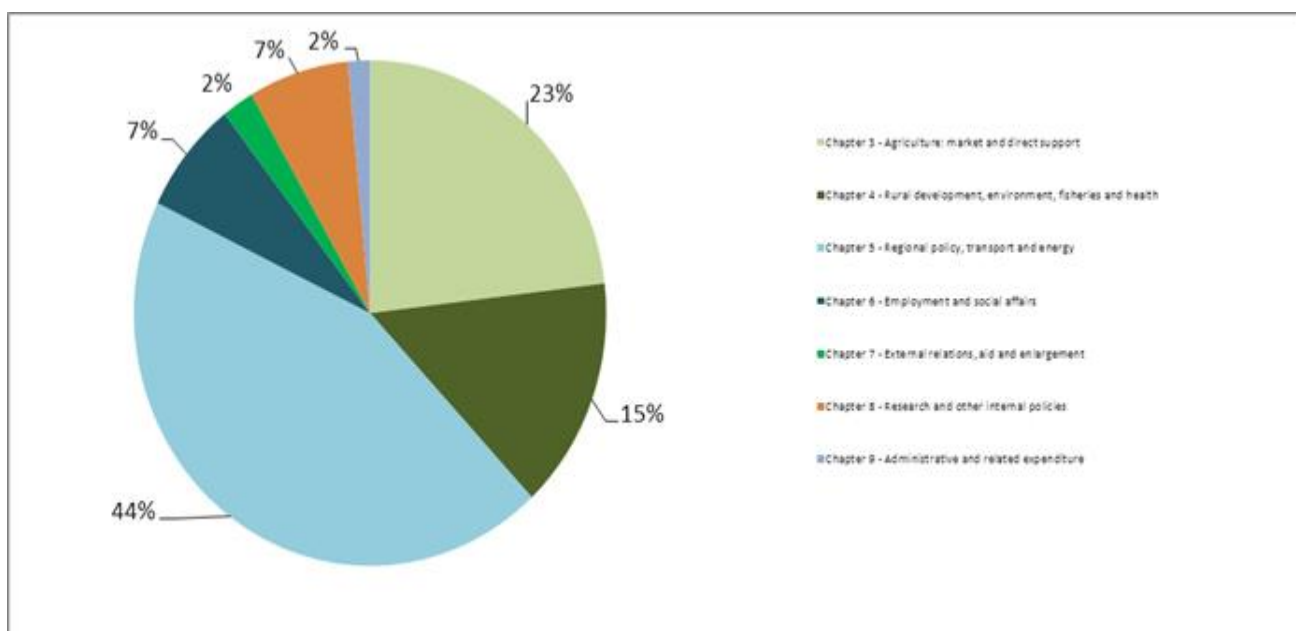
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<sup>2</sup> ECA AR 2013 p. 23.

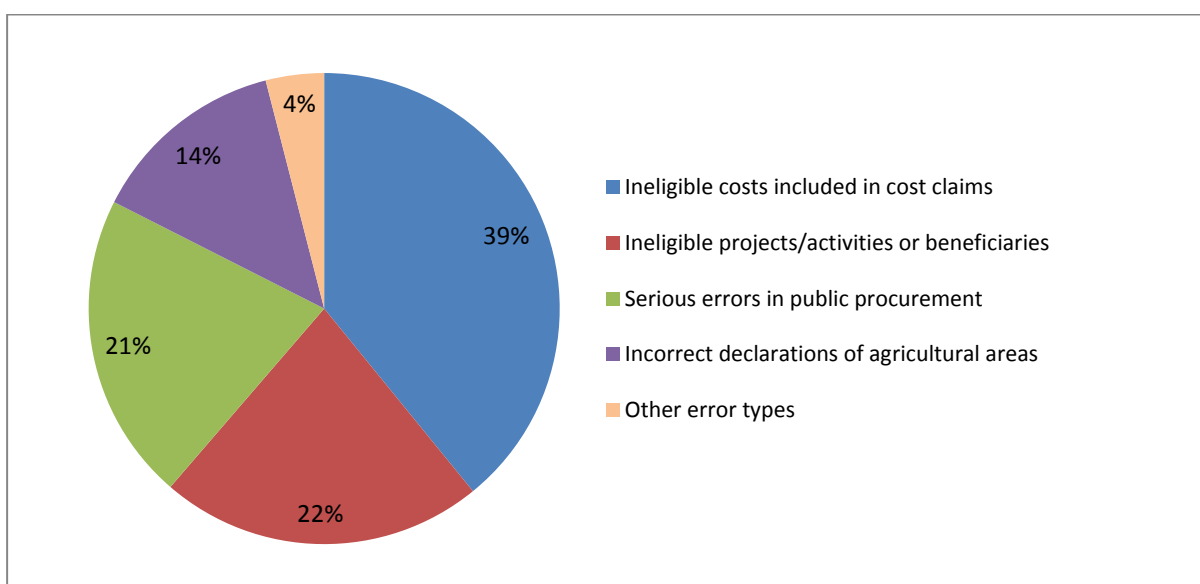
<sup>3</sup> ECA AR 2013 p. 23.

States had sufficient information available to have detected and corrected the errors before claiming reimbursement from the Commission<sup>4</sup>.

The graph below gives a breakdown of the contribution by policy area to the estimated error rate<sup>5</sup>.



With regard to types of errors, the Court's report stated that eligibility errors contributed significantly to the overall estimated error rate. Serious errors in public procurement and incorrect declarations by farmers also accounted for a large proportion of the errors. The graph below provides a breakdown of the contribution of the error type to the overall estimated error rate.



<sup>4</sup> ECA AR 2013 p. 83, p. 111, and p. 153.

<sup>5</sup> ECA AR 2013 p. 26.

### 3 Summary of the Member States' replies

#### 3.1 MAIN QUANTIFIABLE ERRORS IN SHARED MANAGEMENT

During its 2013 audit, the Court identified specific categories of quantifiable errors in shared management which contributed significantly to the most likely error rate for the policy areas concerned. In the policy area Agriculture: market and direct support, overstated number of eligible hectares or animals and ineligible beneficiary/activity/expenditure together contributed 80 % to the most likely error rate.

In Regional policy, transport and energy serious errors in public procurement accounted for 45 % of all quantifiable errors and made up approximately 39 % of the estimated error rate for the policy group<sup>6</sup>. In the policy area Employment and Social affairs errors related to public procurement breaches accounted for 7 % of all errors, which shows that the risk of non-compliance with public procurement is still relevant<sup>7</sup>.

In chapter 3 of its annual report the Court reported on the systematic weaknesses in the Land Parcel Identification System (LPIS) stemming from incorrect assessment of the eligible land in LPIS databases<sup>8</sup>. The Member States concerned were therefore requested to provide information on whether databases were updated and the measures taken by them to solve recurrent problems. All Member States concerned replied that they could now guarantee that LPIS databases are updated on a regular basis and that the LPIS ensures a correct assessment of eligibility of land, and systematically detects over-declarations.

Poland reported that since 2009: "it has been consistently and gradually reorganising the method for updating LPIS data. The main change was the introduction in the production system of on-line reference database updates by ARiMR<sup>9</sup> specialists by means of a dedicated GIS IT tool<sup>10</sup>." Further, the Polish authorities pointed out that "as regards the LPIS-related irregularity found by the Court of Auditors in 2013, it is not true that the irregularity is systemic in nature" and that the Court had incorrectly recognised a part of a parcel flooded in 2013 as ineligible for payment in 2012<sup>11</sup>.

Ireland stated that a review of the LPIS database is an on-going iterative process<sup>12</sup>, while France stated that an Action Plan approved by the Commission and on-going in 2015 has been established in order to update LPIS<sup>13</sup>. Romania mentioned that funding for new orthoimages, as well as new staff and training would be needed to improve the situation.

Finally, Germany underlined the fact that in its case, the over-declaration identified was an individual case "which did not have any financial impact" and that efforts have always been made to ensure that the LPIS is updated properly and on a regular basis<sup>14</sup>.

In Rural development, the Court found serious cases of non-respect of eligibility for investment projects rendering certain types of expenditure ineligible.

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<sup>6</sup> ECA AR 2013, p. 148.

<sup>7</sup> ECA AR 2013, p. 177.

<sup>8</sup> ECA AR 2013, Box 3.1 and Box 3.4.

<sup>9</sup> Agencja Restrukturyzacji i Modernizacji Rolnictwa (ARiMR).

<sup>10</sup> SWD p.143. .

<sup>11</sup> SWD p.143.

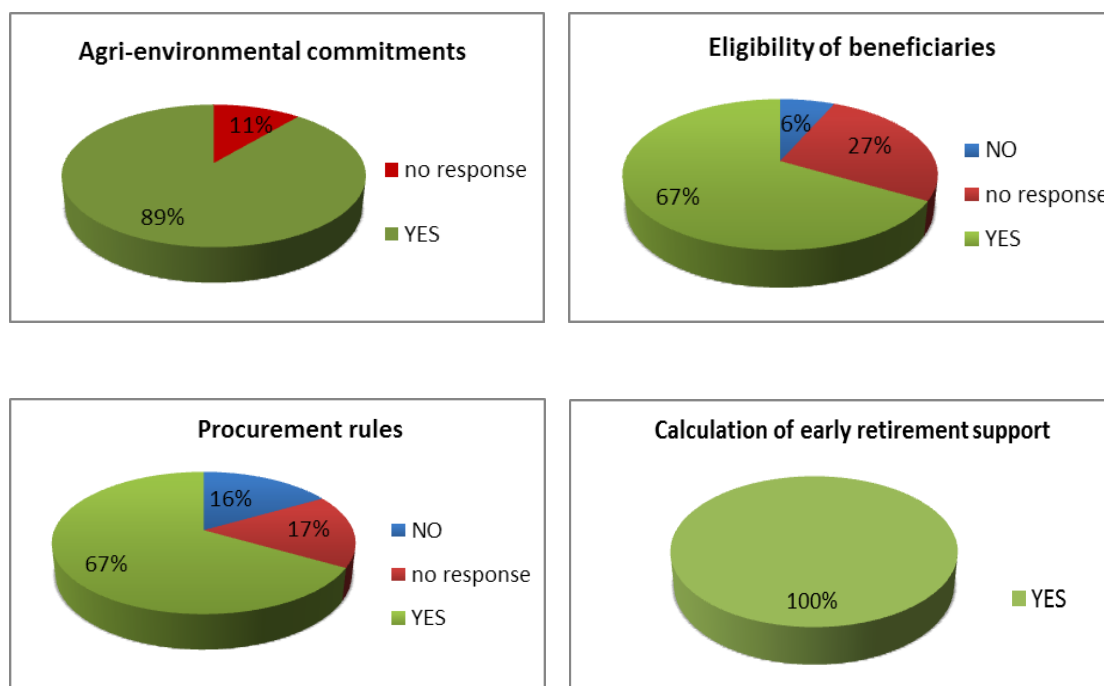
<sup>12</sup> SWD p.118.

<sup>13</sup> SWD Annex 1 and Annex III p33, p106

<sup>14</sup> SWD p.108.

Member States were asked whether they were in a position to state that their control system had addressed the recurrent deficiencies identified by the Court in relation to: agri-environmental commitments, ineligible beneficiaries, non-respect of procurement rules and ineligible support for early retirement.

The Member States concerned stated that they had addressed all or nearly all the identified recurrent deficiencies. The graphs below give an overview of the replies received:



Greece highlighted two areas where it had made significant improvements: an amendment to agri environmental payments which involved redesigning the system of penalties for certain actions and an amendment to national legislation in the field of public procurement<sup>15</sup>.

The Polish authorities stated that with regard to ineligibility of support for early retirement, they disagreed with the Court and with the Commission that "the implementation of the measure 'Structural pensions' involved fraud or another illegal activity detrimental to the financial interests of the Union" As a result, clarifications were submitted and remedial actions were taken by the authorities. The Commission has requested a recovery of the unduly paid amounts.

Regarding the question on public procurement breaches, nearly half of all Member States responded that they had identified systemic issues related to public procurement and that they have taken preventive measures in this context.

Scotland (UK) stated that: "Although we have been active in promoting procurement compliance, we still need to do more to inform the Managing Authority and beneficiaries of the importance of procurement compliance and the impact it can have."

Slovenia reported on three areas of improvement 1) a project group appointed in November 2014 specifically for dealing with questions relating to the field of public procurement, 2) an analysis of public contracts, and 3) Administrative competence

<sup>15</sup> SWD p.112.



(additional employment and training in the public procurement field) has been and will be implemented as part of technical assistance<sup>16</sup>.

Other Member States have undertaken certain measures to try to limit and prevent public procurement breaches. Romania has put in place legislative and systems based measures and the Czech Republic has taken national preventive and corrective measures. Croatia has taken numerous preventive actions including workshops and a training programme of 50 classes leading to the award of a certificate in the area of public procurement, valid for three years<sup>17</sup>. Portugal and Hungary have established Action Plans to improve public procurement, while in Estonia the management and control system in relation to procurements have been "seriously enhanced" in the last few years<sup>18</sup>.

Some Member States however affirmed that they had very few systemic problems with regard to public procurement. Spain asserted that:

"Although various issues have been identified with regard to public procurement, their type varies from body to body and usually affects specific contracts... Furthermore, problems identified in public procurement are not considered to be systemic and in all cases where public procurement irregularities have been identified, the affected expenditure has been withdrawn so that the EU budget will not be affected."<sup>19</sup>

Finland noted that "Compliance with the procurement rules is monitored more closely for aid co-financed from EU funds than in national aid programmes"<sup>20</sup>.

Finally, Germany stated that it had not "identified any system-related problems in terms of the European Social Fund (ESF) in conjunction with public procurement" but had nonetheless in certain cases taken "precautionary measures"<sup>21</sup>.

Member States' replies to issues related to the main quantifiable errors underline the fact that they have been undertaking a series of preventive and remedial actions. In addition, there seems to be a commitment to tackling the systemic weaknesses, thereby reducing the number of quantifiable errors.

### **3.2 ENHANCED ACCOUNTABILITY OF MEMBER STATES- SOUND FINANCIAL MANAGEMENT**

In its 2013 report, for shared management, the Court found that in many cases the national authorities had sufficient information to prevent, detect and correct the errors, before declaring the expenditure to the Commission<sup>22</sup>. The Court has underlined the fact that the EU spends its budget, but there is still significant room for further improving how those funds are spent. Funds should be spent in conformity with the rules while at the same time getting the results expected<sup>23</sup>. This subsection of the report examines replies to questions on Member State accountability with the focus on management and national declarations, management verifications and the role and importance of the Court's assessments.

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<sup>16</sup> SWD p.173.

<sup>17</sup> SWD p.90.

<sup>18</sup> SWD p.103. .

<sup>19</sup> SWD p.177.

<sup>20</sup> SWD p.104.

<sup>21</sup> SWD p.110.

<sup>22</sup> ECA AR 2013 . p. 83, p. 111, and p. 153.

<sup>23</sup> Speech – Presentation of the 2013 Annual reports to the Committee on Budgetary control of the European Parliament- President Caldeira.

76 % of Member States stated that mandatory management declarations could have a positive impact on the prevention, detection and correction of errors by Member States. Hungary affirmed that management declarations have been put in place and that the declarations must be forwarded to the Minister responsible for the State budget<sup>24</sup>.

Scotland (UK) and Latvia both responded that management declarations would have a positive impact, thereby increasing Member State accountability.

When questioned on the subject of the usefulness of national declarations, just over half of all Member States responded favourably. Denmark and the UK, both participants in the inter-institutional working group concerning national declarations made statements in support of national declarations. Denmark remarked that:

"One of the conclusions was that the purpose of national declarations is to ensure greater political responsibility for ensuring the correction of errors in national payments of EU funds. We in Denmark believe that this is an important concept to disseminate and the recommendations form a good starting point for countries which do not yet have a model for this in place. In Denmark, the political level is held accountable, as the Public Accounts Committee annually submits a report on the use of EU funds in Denmark... The Danish model thus ensures accountability regarding the use of EU funds at national political level"<sup>25</sup>.

The UK stated that it supported the recommendations of the working group and that:

"we welcome that these recommendations are suitably flexible, to take into account national circumstances and processes, meaning that Member States have discretion when producing such a voluntary document. We also welcome that these recommendations underline the importance of good reporting to improving the management of EU funds"<sup>26</sup>.

However, criticism of management declarations focused on the fact that they provided no added value, since existing systems were adequate and possibly there would be an increased administrative burden<sup>27</sup>.

Member States not in favour of the idea of national declarations (Latvia and Estonia, for example) made reference to the fact that there may be overlaps with other annual reporting and added bureaucracy<sup>28</sup>. In addition in decentralised (France) and federal countries (Germany) national declarations were regarded as ineffective.

A sizable proportion of Member States (86 %) regarded the results of the Court's assessments as useful and contributing to their own assurance of the legal and regular use of EU funds. Slovakia stated:

"Assessments by the Court of Auditors can deliver relevant stimuli to revise national rules applied by individual entities providing contributions from EU funds. In relation to assessment results regarding systemic or horizontal issues, this is a direct and valuable resource for the implementation of the necessary adjustments and corrective measures at national level"<sup>29</sup>."

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<sup>24</sup> SWD p.117.

<sup>25</sup> SWD- p.102.

<sup>26</sup> SWD- p.181.

<sup>27</sup> SWD- Germany, Ireland, Belgium- p.82, 111, 119.

<sup>28</sup> SWD Latvia and Estonia- p.123, p.103.

<sup>29</sup> SWD- p.169.

Croatia also noted that: "The results of the Court's assessment are taken into consideration and they contribute to the improvement of existing legislation and the prescribed procedures for the use of EU funds<sup>30</sup>."

On the subject of improvement of management verifications, 72 % of Member States responded positively. The Czech Republic and Spain<sup>31</sup> both stated that they had drawn up Action Plans with a view to improving management verifications and in the case of Spain, "as a result of applying these plans, the error rates indicated in the Audit Authority annual control reports have fallen considerably."

Luxembourg listed improved measures which included: working groups with beneficiaries, establishing guidelines and 100 % control of all justifying documents by the Managing Authority, before submitting a payment request to the Commission<sup>32</sup>.

Latvia stated that the Managing Authority regularly draws up a certificate for the Certifying Authority and that the verification system in place is robust. As a result, it has been able to withhold expenditure declarations from two beneficiaries and refer the respective cases to its national fraud office<sup>33</sup>.

Other Member States declared that their verification systems in place were sound as evidenced by a low error rate and therefore there was no need for improvement. This was the case for the Netherlands and Austria<sup>34</sup>.

Concerning accountability, replies from the Member States demonstrate a heightened awareness of the need to be accountable, which is reflected in actions such as the measures undertaken to improve management verifications. Nonetheless, there are concerns about the added value and excessive administrative burden of management and national declarations.

### **3.3 ENHANCED ACCOUNTABILITY OF MEMBER STATES-TOWARDS A GENUINE CULTURE OF PERFORMANCE**

In its 2013 report, the Court found that for the 2007-2013 programming generally the focus was more on the need to spend EU funds in compliance with rules and that the focus on performance was limited<sup>35</sup>.

In this year's questionnaire Member States were asked how they ensured that performance was a key element in the use of EU funds and what measures had been put in place to monitor programme and project performance. A significant majority of Member States provided comprehensive replies to these two questions.

The use of **criteria**, **indicators** and **evaluations** are the means by which many countries ensure performance is a key element. The Netherlands reported that under the ERDF assessment criteria are used in the selection of projects. These include: "contribution to the OP, degree of innovation, quality of the business case and/or

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<sup>30</sup> SWD- p.90.

<sup>31</sup> SWD- p93, p.177.

<sup>32</sup> SWD- p.131.

<sup>33</sup> SWD- p.121.

<sup>34</sup> SWD- p.78,136.

<sup>35</sup> EC AR 2013, p. 257.

business plan, quality of the project and sustainability. Checklists are also drawn up jointly for this purpose"<sup>36</sup>.

Poland stated that it used "weighted criteria" under the Rural Development Programme 2007–2013 and that "the application of the selection criteria is to ensure that projects most likely to contribute to the achievement of the objectives and results set out in the Rural Development Programme are chosen for funding". For the 2014–2020 period, projects will be chosen by applying the "selection criteria".

Romania (AM POSCCE) has combined evaluation with a selection grid and scoring system, thereby ensuring that the best-performing projects receive funding<sup>37</sup>. Belgium (Wallonie) has set up a Task Force of independent experts from the academic and industrial worlds to evaluate the quality of projects proposed. The performance of these projects is also analysed via SMART objectives<sup>38</sup>.

Indicators are used by several Member States. The Czech Republic has established harmonised basic/horizontal rules that cut across operational programmes and a National Code List of Indicators, which contains indicators for all programmes in order to track their progress; Spain makes reference to the Regulation (EU) No 1306/2013 which establishes indicators for the evaluation and monitoring of European Agricultural Fund for Rural Development (EAFRD) as well as European Agricultural Guarantee Fund (EAGF) funds.

Luxembourg provides a clear description of how it ensures that performance remains a core issue. It states that the Managing Authority monitors the operational programme based on clear indicators which are regularly updated. These indicators are reported on in an Executive report. In addition, the application form for projects is designed to verify whether even at the early stage of submission the project is likely to meet the operational programme objectives of the ESF.

In terms of monitoring, **progress reports, control measures, evaluations and tracking of indicators** are among some of the more common measures used by Member States.

Malta clearly outlines the measures it uses for monitoring. They are as follows: 1) structural funds database regularly updated by beneficiaries, 2) project progress reports submitted twice yearly to the Managing Authority, 3) physical spot checks, and 4) project progress meetings with all parties concerned<sup>39</sup>.

The Netherlands, Austria, Latvia and Slovenia all make reference to progress reports or annual reports and reviews as a key means of monitoring performance<sup>40</sup>.

Denmark (Danish Agri-Fish Agency) refers to its comprehensive control measures in place concerning the payment of EU funds for area schemes and non-area schemes. These control measures cover both an administrative and a physical control<sup>41</sup>.

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<sup>36</sup> SWD- p.136.

<sup>37</sup> SWD- p.152.

<sup>38</sup> SWD- p.80.

<sup>39</sup> SWD- p.133 - 134.

<sup>40</sup> SWD- p.77, 120, 136, 171.

<sup>41</sup> SWD- p.98.

Bulgaria (OPRD) lists its control measures and states that the general terms in agreements for granting financial support include the following requirements 1) the beneficiary shall carry out and document three inspections on the physical condition of investments, 2) the beneficiary shall report the results of such checks to the Contracting Authority, and 3) the beneficiary shall not transfer its ownership of the facility built with the investment under this Agreement.

The Czech Republic states that at least one project indicator must be tracked and projects without indicators are inadmissible.

Overall Member States have affirmed their commitment to performance. The lessons learnt as well as the best practices from the previous programming period are already being put into action during this new programming period. The Czech Republic states that it will put in place a "new development" for 2014-2020 which will entail a more detailed project description clearly reflecting the likely projected results while Estonia will place a "special focus" on performance indicators for the new programme period.

#### **4. CONCLUSION**

In its report for the DAS year 2013, the Court remains critical of the high number of quantifiable errors in shared management. As in 2012, the Court has again underlined the fact that for a large proportion of transactions affected by error, Member States authorities had sufficient information to have detected and corrected these errors before claiming reimbursement. In addition, the Court emphasised the need for more attention to be paid to getting the best results possible with limited funds. The Court recommends greater emphasis on performance.

In their replies to the three questionnaires, Member States provided evidence of their continued actions to reduce the number of errors in shared management. Action Plans in both the policy areas Agriculture and Cohesion have been established by several Member States in partnership with the Commission. Regarding procurement many Member States admitted to be affected by systemic issues, but they also emphasised that there have been many preventive and corrective actions.

Member States have in general embraced the concept of greater accountability. Generally management declarations are considered as having a positive impact, while national declarations, although less popular, have been regarded as beneficial.

Finally, the commitment to performance at Member State level can be illustrated by Denmark's closing comment:

"It is Denmark's belief that a pivotal aspect of a satisfactory implementation of the EU budget is that results are achieved. It is therefore important that a framework is created for a results-oriented system which focuses to a greater extent on the results and effects of EU projects. We in Denmark also believe it is important to create transparency concerning the EU added value that the funds create. Denmark wishes the discussions concerning the attainment of results to help strengthen the link between the result evaluations and the budget-related and legal regulation of the various policy areas<sup>42</sup>."

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<sup>42</sup> SWD- p.182.